COLUMBIA THREADNEEDLE
INVESTMENTS

THE LINGERING EFFECTS OF THE FINANCIAL CRISIS — OVER 10 YEARS LATER

More than a decade into the recovery that followed the Great Recession of 2008–2009, many market commentators believe we're in the late stages of the economic cycle that began as the crisis started to recede. As financial markets watch for early indications of change on the horizon, the economic environment still bears the imprint of the events that unfolded in the aftermath of the Great Recession.

Highly unorthodox central bank policies intended to provide what former U.K. Chancellor Alistair Darling has called "short-term shock therapy" have evolved into our new normal. There's no doubt that these monetary policies in the immediate aftermath of the crisis, such as quantitative easing, or the practice of increasing the supply of money to stimulate economic activity, helped to stave off a potential depression.

But our inability to dispense with these crisis-era measures is undermining confidence in the strength of the recovery and encouraging a continuing sense of fragility.

Here are six ways the consequences of the Great Recession continue to dominate our outlook and define the room for maneuvering.

1. Debt has continued to pile up

Other than a brief pause during the worst of the crisis, the global stock of debt has continued to grow, aided by two events: the sharp drop in interest rates by the major central banks from 2008 on and the introduction of quantitative easing.

Having reached around $180 trillion on the eve of the crisis, the debt has since climbed to about $250 trillion.[1] If excessive debt was partly responsible for the Great Recession, there's no sign that this problem has been resolved. Rather, its focus has shifted from private to public sector balance sheets.

The U.S. economic recovery following the Great Recession is the longest on record, but it's also one of the weakest.

2. Too Big to Fail lives on

The term Too Big to Fail (TBTF) predates the Great Recession — but it gained new meaning during the financial crisis; it became clear that the banking system is so interconnected that a crisis in one area can easily engulf the whole. Today, governments and regulators have done what they can to manage the risks of TBTF: identifying systemically important institutions for additional oversight, mandating resolution plans for failing banks and carrying out rigorous stress testing of assets and liquidity.

3. Productivity and labor force growth have stalled

Since the Great Recession, productivity growth in developed economies has slowed sharply. Weak labor force growth has led to tight employment markets and skills shortages, a growing problem in Europe and Japan and particularly noticeable in the U.S. These two factors tend to impede consumption and encourage increasing leverage.

4. China's influence over the world economy has grown

As China's economy has claimed a steadily larger share of world economic output, the rest of the global economy has become increasingly sensitive to slowdowns in China's pace of growth. Concerns have also grown over the country's spiraling stock of debt. China protected its economic expansion during the Great Recession with the biggest stimulus package enacted in any country, largely channeled through its state-owned banks.

Banking assets almost doubled to 250% of gross domestic product (GDP), and debt exploded from 248% of GDP to 441% by September 2018.[2] China has never exerted greater influence over the direction of the global economy.

Source: Columbia Threadneedle Investments as of July 2019. Past performance does not guarantee future results.

5. Economic recovery left too many behind

The U.S. economic recovery following the Great Recession is the longest on record, but it's also one of the weakest. In contrast, the U.S. stock market has staged one of the strongest recoveries on record, benefiting owners of capital but contributing to increasing income inequality in the U.S. In 1970, family income at the 90th percentile was seven times higher than at the 10th percentile. By 2016, the gap had jumped to 13 times — family income at the 10th percentile showed almost no growth over that period.[3] Growing income inequality across the developed world has likely contributed to the rise of populist politics around the globe.

6. Globalization has petered out

The coordinated global reaction to the Great Recession was a prime example of international cooperation through multilateral organizations set up following WWII. But today, nationalistic politics dominate. Countries like China and Russia are asserting their "great power" status more aggressively; narrow self-interest dominates international relations. As a result, the globalization that drove much of the world's economic growth in the decades leading up to 2008 has ground to a halt. If another crisis were to take hold, it's not clear that countries would necessarily rekindle their former spirit of cooperation and connectedness.

Lessons learned

These are some of the major legacies of the Great Recession. But with hindsight, what lessons should we take from it for the future? One clear conclusion is that countries that took swift, decisive action to address their problems reaped big benefits. The U.S.' enforced recapitalization of its banking system allowed it to recover quickly and increase its support for the real economy.

European banks are still gradually recapitalizing themselves more than 10 years later, leaving European companies, which are heavily reliant on bank finance, at an obvious disadvantage. The U.S.' economic outperformance relative to Europe since the Great Recession is arguably due in part to its robust banking sector, which supports the real economy in a way European banks cannot.

A second conclusion is that well-intentioned regulation in response to a crisis can sow the seeds of problems in the future. The Volcker Rule reduced the willingness of fixed-income market makers on Wall Street to carry inventory the way they had before the Great Recession. Rules intended to make Wall Street banks safer have increased the risk that fixed-income markets could see their liquidity dry up during periods of stress.

Bottom line

The Great Recession may have given way to a period of sustained economic growth, especially in the U.S., but the crisis continues to cast a long shadow. As the world economy moves into its second decade of expansion, the effects of the previous crisis are still plain to see.

By keeping a close eye on the economic triggers that preceded the Great Recession, learning from previous mistakes and acting swiftly to resolve brewing financial issues, world leaders can help ensure that history does not repeat itself.

[1] Bloomberg as of 11/14/19

[2] Bloomberg banking assets represented by aggregate assets and liabilities of banks within China

[3] A Guide to Statistics on Historical Trends in Income Inequality, August 21, 2019

Columbia Threadneedle Investments is a leading global asset manager that provides a broad range of investment strategies for individual and institutional clients. With over 450 investment professionals across 17 countries, we manage $469 billion* across asset classes. Our global investment team debates and challenges their best ideas to make better decisions, leading to better outcomes for you and your clients.

To find out more, call **800.426.3750**
or visit **columbiathreadneedle.com**

The views expressed are as of the date given, may change as market or other conditions change and may differ from views expressed by other Columbia Management Investment Advisers, LLC (CMIA) associates or affiliates. Actual investments or investment decisions made by CMIA and its affiliates, whether for its own account or on behalf of clients, may not necessarily reflect the views expressed. This information is not intended to provide investment advice and does not take into consideration individual investor circumstances. Investment decisions should always be made based on an investor's specific financial needs, objectives, goals, time horizon and risk tolerance. Asset classes described may not be suitable for all investors. Past performance does not guarantee future results, and no forecast should be considered a guarantee either. Since economic and market conditions change frequently, there can be no assurance that the trends described here will continue or that any forecasts are accurate.

* In U.S. dollars as of September 30, 2019. Source: Ameriprise Q3 Earnings Release. Contact us for more current data.

Investment products offered through Columbia Management Investment Distributors, Inc., member FINRA. Advisory services provided by Columbia Management Investment Advisers, LLC.

Columbia Management Investment Distributors, Inc., 225 Franklin Street, Boston, MA 02110-2804

Columbia Threadneedle Investments (Columbia Threadneedle) is the global brand name of the Columbia and Threadneedle group of companies.

© 2020 Columbia Management Investment Advisers, LLC. All rights reserved.

CT-MK/**115403 A (01/20)** KRV4/2899498